

By J. David Hulchanski

# Tax Costs of Housing

*We need improved social housing programs, not private sector subsidies and tax remissions which aid investors and wealthier homeowners*

With the release of the *Consultation Paper on Housing* last January, the federal government announced that it is providing Canadians with a "starting point for a fundamental review of housing policy." The paper is supposed to help "ensure a complete and balanced public discussion on housing and the role of government."

Such a thorough review of housing policy is long overdue. Housing Minister McKnight should be congratulated for initiating this public process, something his predecessors should have done. However, the government's consultation paper provides a less than satisfactory start for such a review and, in places, the information is definitely misleading.

In the course of the cautiously written text, the cost and targeting of social housing programs receive particular attention. The first table, for example, shows current and projected federal housing expenditures, yet ignores the costs of the private sector subsidy programs of recent years, as well as the cost of federal housing tax expenditures. This allows the government to indicate, at the start of the paper, that over 60 percent of federal housing expenditures are for social housing. Furthermore, the paper implies that, if we allow things to continue as they are, social housing will swallow up 80 percent of the housing budget in two years.

Such a claim, however, is a serious distortion. The careful reader will find the footnote to Table 1 that states "the table does not include federal tax expenditures related to housing." One must also know a great deal about recent housing program trends in order to realize that 1984/85 is a unique budget year in terms of housing subsidies. For one of the first times in the past two decades, there are no direct subsidy programs for private sector rental or ownership housing. This is due in part to the relatively low interest rates at the

moment, in part to the large federal deficit and in part to the widespread recognition that these programs have been wasteful.

Almost all the benefits of these programs have gone to higher income homeowners and to real estate investors.

By focusing on the cost of the one program which provides assistance to low and moderate income renters, the paper presents a very narrow definition of the housing problem as seen from the perspective of the government's budgetary priorities. This certainly should not be a surprise.

What is surprising is the degree to which an attempt has been made to avoid saying anything of substance about future directions while still conveying the basic message of both the Conservative government and the private sector housing lobby. The basic theme is the high cost of social housing and the tremendous drain on the budget caused by continuing this supposed 60 percent of federal housing subsidies.

There is yet a further issue underlying this preoccupation with social housing spending. It is the issue of targeting. Here we find a cousin of the universality debate. Though the social housing programs are not universal, they do house both low and moderate income households to achieve a social mix. The programs do not limit themselves to the "truly needy."

As is the case with universal social programs, this creates ideological problems for many conservatives, not to mention the entrepreneurs in private sector housing who view these programs as competition with their potential market. Social mix also poses problems for many traditional market economists who question the economic efficiency of any form of direct government activity in the marketplace.

Finance Minister Michael Wilson, for example, made clear in his November 1984 *Agenda for Economic Renewal*

that we "should ensure that those who receive federal housing assistance are truly in need of such assistance."

Frank Clayton, a housing economist and key policy consultant to the private sector housing lobby, urges the targeting of housing subsidies "at those in need and only those in need."

Housing Minister McKnight echoed these sentiments when he addressed the annual meeting of the Canadian Home Builders Association a few days after the release of his consultation paper. He told the home builders that he is "going to look at all of our housing programs to make sure that they are targeted to the people who need them most."

In terms of directing assistance to lower income Canadians, our system of housing subsidies and incentives is one of the more, if not the most regressive categories of federal expenditures. The expenditure on the current social housing programs is not only one of the smaller spending items in our system of direct and indirect housing subsidies, it is also the federal government's only significant housing program focused on assisting low and moderate income renters. Unfortunately, when the housing minister states that he is looking at "all" housing programs he is only referring to one category of expenditures, direct expenditures (cash subsidies) rather than indirect expenditures (subsidies via the tax system).

Aside from mentioning housing-related tax expenditures in a footnote, there is no further elaboration of just what this spending category is, or how extensive and expensive an item it might be. Passing reference is made to the cost of one form of housing tax expenditure, the \$125 million annual cost of the Registered Home Ownership Savings Plan (RHOSP). The paper fails to note that in order to take advantage of RHOSP one must have enough income to be able to afford to lock away up to \$1,000 per year and have a secure,

higher-paying job sufficient to hope eventually to become a homeowner. In other words, low income renters need not apply.

Though one other housing tax expenditure program is mentioned, the Multiple Unit Residential Building (MURB) program, its cost and beneficiaries are not. This one rental supply subsidy program alone has cost the federal government over \$1 billion in foregone revenues (and another \$500 million in foregone provincial revenues) over the past eight years. We will continue paying for the MURB program for many years to come. Since low and moderate income Canadians are not in the higher tax bracket, the MURB program had no direct benefits for them and only a small percentage of renters can even afford the expensive condominium-type units built by the wealthy MURB investors.

The same holds true for the subsidies provided to private builders in the Assisted Rental Program (ARP) and its most recent version, the Canada Rental Supply Plan (CRSP). Virtually all the rental units produced by the MURB, ARP and CRSP programs rent at the higher end of the market. Most units built with subsidies from these programs are registered as condominiums to permit easy conversion and sale to individual owners. Not only have these programs failed to help those "truly in need," they do not even contribute to the nation's permanent stock of rental housing. In fact, building sites for MURB, ARP and CRSP projects have often become available through the demolition of existing rental buildings.

The 1982/83 Canada Home Ownership Stimulation Plan does not rate discussion in the consultation paper even though it cost some \$850 million over a fifteen month period. CHOSP distributed \$3,000 grants to the middle and upper income households lucky enough to be able to afford the purchase of a house.

Should these programs be ignored in the "consultation process" as past history, as part of the long gone "bad old days"? Far from being long gone, it will only take a sharp rise in interest rates or a slump in housing starts for programs aimed at market stimulation to be reinstated. Housing is too important a sector in our economy and has far too many ramifications to allow it to languish for very long.

These private market housing supply programs have not contributed to a

healthier private sector nor have they provided any assistance to the "truly needy." In 1982, for example, in response to the high interest rates and a potential severe slump in housing starts, the government created or expanded programs such as CRSP and CHOSP. This resulted in CMHC's loans, grants and subsidies to market housing (\$885.8 million) surpassing the amount provided to social housing (\$747.7 million).

These figures are only the direct expenditures for 1982. They do not include the estimated \$150 million cost of the MURB program, the \$125 million cost of the RHOSP program, or the rest of the housing subsidies delivered through the tax system. Very little of our direct spending on housing provides assistance to low and moderate income Canadians. The distributional impact of indirect spending, housing tax expenditures, is even worse.

The consultation paper notes that the public debate "as to whether federal housing assistance is directed to those most in need" must "be resolved so that certainty and clarity of direction can be provided once again." The average dollar benefits per tax filer from federal housing tax expenditures should have been among the forty six tables in the consultation paper.

Table 1 in this article, from the Department of Finance, provides a sum-

mary of who benefits from the other, or "hidden," housing budget. In his 1984 report to the House of Commons, Auditor General Kenneth Dye refers to the "massive impact" of tax expenditures which "are a huge hidden budget in the financial affairs of Canada." For every \$100 spent directly, Dye estimates \$30 to \$50 is spent indirectly by way of tax expenditures.

As the figures in Table 1 from the 1979 Department of Finance tax expenditure accounts indicate, the greater one's income, the greater the housing tax expenditure benefits received.

We do not have more recent official estimates of tax expenditures, because the Liberal government and now the Conservative government have refused to compile and publish up-dated tax expenditure accounts. In contrast, since 1974, the U.S. Congress has required the tax expenditure accounts to be published annually as part of the U.S. federal budget.

It is not only the regressive nature of housing tax expenditures, but their size relative to direct housing expenditures, which ought to have been one of the issues raised in the consultation paper. Housing tax expenditures are some two to three times greater than the direct spending programs on housing.

In most other sectors, the relationship between the two types of spending is just the opposite—tax expenditures are

**TABLE 1**  
**AVERAGE DOLLAR BENEFITS PER TAX FILER**  
**FROM FEDERAL HOUSING TAX EXPENDITURES, 1979**

Total Income Group	Average \$ Benefit from Housing Tax Expenditures
Under \$ 5,000	\$ 32
5,000 - 10,000	171
10,000 - 15,000	314
15,000 - 20,000	619
20,000 - 25,000	964
25,000 - 30,000	1,312
30,000 - 50,000	1,994
50,000 - 100,000	3,670
\$100,000 & over	6,753

SOURCE: Canada, Department of Finance (1981) *Analysis of Federal Tax Expenditures for Individuals*, Ottawa, p. 12.

less, (between 30 percent and 50 percent according to the Auditor General) than the direct expenditures. Not in housing. For every \$100 in direct housing expenditures, some \$200 to \$300 is spent through housing tax expenditures.

One indicator of the distributional impact of the total package of housing subsidy programs over the past fifteen years can be obtained by examining trends in the distribution of home ownership among income groups. Table 2 demonstrates a most disturbing and very dramatic trend among home ownership patterns—and it is data the consultation paper does not provide.

Because access to home ownership is one of the primary objectives of housing policy, we have had a number of costly programs aimed at stimulating ownership. CHOSP is only the most recent example. There has been the Assisted Home Ownership Program during the 1970s as well as several federal and provincial first-time home buyer grant programs similar to CHOSP. In 1972 the decision was made to exempt a principal residence from capital gains taxes.

As national policy, we have made home ownership an irresistible option. Where else can consumers obtain a \$100,000 asset for about 10 percent down, obtain government grants subsidizing its purchase, receive considerable utility from it, benefit from inflation, receive mortgage assistance when interest rates sky rocket, obtain insurance protection against higher interest rates at mortgage renewal time, and be able to sell it with no taxation on the capital gain?

What has been the distributional outcome of this focus on home ownership? As in the other expenditure categories, it is the wealthy who have gained the most over time. Table 2 clearly demonstrates the gains among the top two income quintiles and the decline among the bottom two quintiles.

This trend, of course, is not due solely to housing programs. Macro-economic conditions continue to work against lower income households and especially those who are not currently owners. The point is that the consultation paper does not even mention this very significant trend toward the increasing polarization of income groups by tenure.

The increase in rates of home ownership among the upper income groups also indicates an equally significant and very troubling trend for the rental housing sector. The rental sector is

increasingly becoming a residual one, containing virtually all lower income Canadians and very few higher income Canadians. This was not always the case.

Table 3 indicates that as recently as 1967 the tenant population was divided almost equally between each of the income quintiles. The only exception was the highest quintile. By 1982, however, the number of higher income tenants (tenants with incomes in the fourth and fifth quintiles) has declined while the number of lower income tenants (tenants with incomes in the first and second quintile) has increased, both by significant amounts for such a short period of time. This means that those households able to take advantage of the home ownership option have done

so, leaving virtually all those who have no choice in the rental sector.

Is it any wonder that private investors cannot supply new rental stock and make money? How can we have a viable private market in a very expensive consumer good when the income profile of the consumers of this commodity is increasingly limited to the lowest income groups?

The private rental sector has not functioned as a private market for the past decade and most likely cannot function in the future, due to the upward cost pressures on supplying a rental unit and the downward trend in the income profile of renters. There are not enough tenants with the incomes necessary to support the economic returns required to make most new

**TABLE 2**  
**CHANGES IN HOME OWNERSHIP RATES WITHIN AND BETWEEN**  
**INCOME QUINTILES**  
**1967, 1973, 1977, 1981**

	% of Households Owning Their Unit				Change 1967-1981
	1967	1973	1977	1981	
Lowest Quintile	62.0%	50.0%	47.4%	43.0%	-19%
Second Quintile	55.5	53.6	53.3	52.4	- 3%
Middle Quintile	58.6	57.5	63.2	62.7	+ 4%
Fourth Quintile	64.2	69.8	73.2	75.0	+11%
Highest Quintile	73.4	81.2	82.3	83.5	+10%
Total	62.7	62.4	63.9	63.3	+0.6%

Sources: Statistics Canada (1983) *Household Facilities by Income and Other Characteristics*, Ottawa: Supply and Services, Catalogue 13-567.

**TABLE 3**  
**RENTER HOUSEHOLDS BY INCOME QUINTILE**  
**Canada, 1967, 1973, 1977, 1981**

Income Quintile					Change 1967-1981
	1967	1973	1977	1981	
Lowest Quintile	20.4%	26.6%	29.1%	31.1%	+10.7%
Second Quintile	23.9	24.7	25.9	26.0	+ 2.1%
Middle Quintile	22.2	22.6	20.4	20.3	- 1.9%
Fourth Quintile	19.2	16.1	14.8	13.6	- 5.6%
Highest Quintile	14.3	10.0	9.8	9.0	- 5.3%
Total	100.0	100.0	100.0	100.0	

Source: Statistics Canada (1983) *Household Facilities by Income and Other Characteristics*, Ottawa: Supply and Services, Catalogue 13-567.

rental projects viable.

When government and housing industry officials voice their concerns about the "truly needy" they are right about one thing—there is a host of very serious inequities in our system of housing subsidies. However, the focus of the consultation paper, social housing programs, may well contain the least of these inequities.

The policy agenda flowing from the consultation paper's narrow formulation of the problem is that we cut back or abolish social housing programs and distribute at least some of these funds on the basis of a means test to certain categories of the "truly needy." This is quite simply an attack on low and moderate income tenant households. The one program which directly assists tenant households is already underfunded and threatened, while the rest of the housing subsidy system is barely mentioned.

This agenda follows Ronald Reagan's and Margaret Thatcher's approach to public policy: a greater reliance on market forces and a sharper targeting of subsidies to, in Reagan's words, "the truly needy." Because Reagan and Thatcher have been in office for several years, analysts are now able to begin measuring the social and economic consequences of their housing policies. What these analysts find is not very encouraging.

The result of the attack on social housing spending in the U.S. and Britain has been to (1) reduce subsidies to tenant households by imposing means tests and (2) eliminate non-market forms of housing supply programs. "No efforts have been made," reports the *Journal of the American Planning Association*, to reduce "the regressive nature of [housing] tax expenditures, or the inequities between renters and owners" in the USA or Britain.

Have these findings any relevance in the Canadian context? The focus of the current debate in Canada has carefully been limited by government and the housing industry lobby to one form of federal housing subsidy, the social housing supply programs. As in the USA and Britain, the public is not given a complete picture of the costs and distributive impacts of all housing programs.

The moderate income renters who benefit from the social housing subsidies—the target of claims that the program is inefficient because these residents are not among the "truly

needy"—are doing the Canadian taxpayer a favour by not taking advantage of the housing tax expenditures as well as occasional programs like CHOSP. The mortgage assistance received by these households in co-op housing projects decreases continually for about 15 years and then ceases. This is the only subsidy a moderate income household receives.

What all this shows is that the *real* issue of the current housing debate is not the "truly needy." It is whether ordinary citizens will be subsidized or whether real estate investors will be subsidized. This is an issue the authors of the consultation paper did their best to avoid.

In immediate practical terms, the major problem with the social housing programs is not that they are a major contributor to the deficit, but that they are one of the remaining discretionary direct spending programs in the housing sector available to Finance Minister Wilson to help him achieve his "economic renewal" through budget cuts. This seems to provide the most plausible explanation of what is contained, and what is not contained, in the consultation paper.

A significant proportion of future housing supply will have to be subsidized. This cannot be avoided. It is indeed time for a thorough review of housing policy. A consultation process would be helpful as long as all the cards are placed on the table and careful consideration is given to the complete

range of housing issues options and policy instruments.

At its most fundamental level, the housing policy option we, as a nation, must address is whether we take a "social welfare" approach to our housing problems or a "market welfare" approach. In other words, do we subsidize improved forms of social housing which directly benefit low and moderate income renter households, or do we continue to subsidize investors, as a form of "market welfare," hoping this incentive to the wealthy will eventually trickle down to the "truly needy." The latter option has not worked in the past. It is not working in Ronald Reagan's America or Margaret Thatcher's Britain. We should not expect it to work in Brian Mulroney's Canada. The one message conveyed by the *Consultation Paper on Housing* is that the government is preparing us for a Reagan/Thatcher approach to Canadian housing policy. ☐

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